DOCUMENT RESUME

ED 396 621 HE 029 251

TITLE	State University of New York Health Science Center at Syracuse Leasing Practices. Report No. 95-S-80.
INSTITUTION	New York State Office of the Comptroller, Albany.
PUB DATE	30 May 96
NOTE	25p.
PUB TYPE	Reports - Evaluative/Feasibility (142)
EDRS PRICE	MF01/PC01 Plus Postage.
DESCRIPTORS	Accountability; Bids; Conflict of Interest; Contracts; *Cost Effectiveness; Decision Making; *Educational Economics; *Educational Facilities Improvement; Educational Finance; *Financial Policy; Higher Education; *Public Colleges; School Accounting
IDENTIFIERS	*Leasing; *State University of NY Health Sci Ctr Syracuse

ABSTRACT

This document presents results of an audit of the leasing practices of the State University of New York (SUNY) Health Science Center at Syracuse covering the period April 1, 1993 through June 30, 1995. The audit investigated whether the Center and the Center's Clinical Practice Management Plan members engage in appropriate and economic leasing practices and whether the Center exercises adequate control over costs related to renovations of leased property. Findings indicated the following: that Center controls over leases are not adequate to ensure that leases are free from conflicts of interest and are obtained at the most reasonable cost; that controls over renovations should be strengthened to reduce the State's cost for improvements to leased properties; that the Center lacks adequate information about the scope and cost of proposed renovations; that the lease decision-making process is not fully documented; that there is a need for a clearly articulated conflict of interest policy; that Plan and State space leases at the Center should be subject to competitive bidding; and that these leases are finalized without assistance from independent experts. Recommendations to correct these inadequacies are given. Also included are comments of SUNY officials who concurred with the recommendations and indicated steps taken to implement them. (CK)

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State of New York
Office of the State Comptroller

Division of Management Audit

Report 95-S-80

Dr. Thomas A. Bartlett
Chancellor
State University of New York
State University Plaza
Albany, NY 12246

Dear Dr. Bartlett:

The following is our audit report on procedures and controls related to leasing of physical space by the State University of New York Health Science Center at Syracuse.

This audit was performed pursuant to the State Comptroller's authority as set forth in Section 1, Article V of the State Constitution and Section 8, Article 2 of the State Finance Law. Major contributors to this report are listed in Appendix A.

Office of the State Comptroller
Division of Management Audit

May 30, 1996

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Executive Summary

State University of New York
Health Science Center at Syracuse
Leasing Practices

Scope of Audit

The mission of the State University of New York (SUNY) Health Science Center at Syracuse (Center) is to provide essential community health care, to educate health care professionals and to conduct research. The Center is made up of four colleges and maintains a 350-bed hospital. The SUNY Board of Trustees' Policy (Policy) requires that medical doctors who work at the Center belong to the Center's Clinical Practice Management Plan (Plan) if they have private practices. The Plan's 22 medical service groups, representing the various medical specialties, must adhere to the Policy.

The Center uses State-owned buildings, and also rents additional space for medical clinics, office space, parking and storage. In 1994, the Center spent $1.7 million in State funds to rent 17 such properties. In addition, 15 medical service groups in the Plan reported spending nearly $2 million to lease space in 1994. Plan groups use their medical practice revenues to pay for these expenses, but must remit revenues that remain at year end to the Center's School of Medicine. The Center and the Plan report that, since 1990, they have also spent $1.8 million to renovate leased space.

We audited the Center's controls over leases for the period April 1, 1993 through June 30, 1995. Our audit addressed the following questions:

- Do the Center and its Plan members engage in appropriate and economic leasing practices?

- Does the Center have adequate controls over costs related to renovations of leased property?

Audit Observations and Conclusions

We found that Center controls over leases are not adequate to ensure that Center and Plan leases are free from conflicts of interest and are obtained at the most reasonable cost. We also found that controls over renovations should be strengthened to reduce the State's costs for improvements to leased properties.

According to Center officials, the Center and Plan groups try to lease space around the Center in the "University Hill" area of Syracuse so that the properties are convenient for students, instructors and clinical practitioners. This need for proximity to the Center may create a market

demand for such properties, some of which are owned by individuals with affiliations with the Center.

Our audit found that, for some of the leases we reviewed, the landlord was a Center (State) employee, or an employee of the Plan affiliated with the Center. The State Public Officers Law prohibits State employees who own businesses from doing business (over $25) with the State unless competitive bidding is used to ensure that rates are reasonable and the award is free from favoritism. However, Center officials stated that they did not use competitive bidding procedures until recently. In addition, we found that the Center has no conflict of interest policy to guide lease decision making and does not adequately document the reasons lease decisions are made. On June 27, 1995 the SUNY Board of Trustees adopted an overall conflict of interest policy.

When we examined leases at one of the locations noted above, we found that the Center and the Plan had paid $1.4 million ($24.66 per square foot) in 1994 to lease property owned by two members of a Plan group. In 1995, the Center was able to rent property in the same neighborhood at a rate of $17 per square foot. The 1995 lease agreement represents the first time the Center used competitive bidding procedures to obtain a lease. Center officials maintained that all lease rates were reasonable as supported by an independent appraisal for one location. However, we do not believe that an appraisal can establish the reasonableness of Center and Plan leases given the potential conflict of interest and leasing control weaknesses which existed.

Our audit also showed that the Center may not have adequate information about the scope and cost of proposed renovations to be able to determine their value. The Center and some Plan groups rely heavily on the landlords to determine the value of these projects. The Center does not use available independent experts in evaluating renovation proposals, and does not negotiate lease terms that protect the State's investment in renovations made to leased space.

Comments of SUNY Officials

SUNY Officials concur with our recommendations and indicate steps are being taken to implement them.

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Introduction

Background

The Health Science Center at Syracuse (Center) has a threefold mission: to provide essential community health care, to educate health care professionals, and to conduct research. The Center is made up of four colleges: the College of Health Related Professions, the College of Medicine, the College of Nursing and the College of Graduate Studies. The Center also operates a 350-bed hospital.

The State University of New York (SUNY) Board of Trustees' Policy (Policy) requires that medical doctors who work at the Center belong to the Center's Clinical Practice Management Plan (Plan) if they have private practices. The various medical specialties are organized into medical service groups. There are 22 medical service groups within the Center's Plan. Although each medical service group in the Plan operates as an independent business, it must adhere to the Policy. The Policy provides that any unspent Plan revenue each year accrues to the Center's School of Medicine. These funds are then spent for the benefit of the School of Medicine subject to the approval of the Center's President.

To meet the needs of its patients and its health care professionals, the Center has found it necessary to lease space in addition to the available space in State-owned buildings. Currently, the Center has 17 such leases paid with State-appropriated funds. During 1994, State lease payments totaled over $1.7 million. The Center uses the leased space for medical clinics, office space, parking and storage.

The individual medical service groups within the Center's Plan may expand their private medical operations as they see fit. The groups pay the leases from revenue generated in treating patients. In 1994, 15 medical service groups reported paying some rental expense, which collectively totaled nearly $2 million.

Audit Scope, Objectives and Methodology

We audited the Center's procedures and controls related to property leases for the period April 1, 1993 through June 30, 1995. The objectives of our performance audit were to determine whether the Center and its Plan members engage in economic and appropriate leasing practices, and whether the Center has adequate controls over costs related to renovations of leased space.

To accomplish our objectives, we interviewed administrative staff, and reviewed leases paid with State funds and selected leases paid with Plan funds. In addition, we compared Center and Plan lease costs with the costs of other commercial property leases in Syracuse. We also utilized the services of officials at the State Office of General Services (OGS) and Department of Health (Health) in reviewing the lease agreements.

In addition, we reviewed controls and procedures associated with projects to renovate leased space. Our audit focused on the process followed by the Center and the Plan once the need for space had been determined, and did not include examining the basis on which this determination was made.

We conducted our audit in accordance with generally accepted government auditing standards. Such standards require that we plan and perform our audit to adequately assess those operations of the Center which are included within our audit scope. These standards require that we review and report on the Center's internal control structure and its compliance with those laws, rules and regulations that are relevant to those operations that are included in our audit scope. An audit includes examining, on a test basis, evidence supporting transactions recorded in the accounting and operating records, and applying such other auditing procedures as we considered necessary in the circumstances. An audit also includes assessing the estimates, judgments, and decisions made by management. We believe that our audit provides a reasonable basis for our findings, conclusions and recommendations.

We use a risk-based approach when selecting activities to be audited. This approach focuses our audit efforts on those operations that have been identified through a preliminary survey as having the greatest probability of needing improvement. Consequently, by design, finite audit resources are used to identify where and how improvements can be made. Thus, little audit effort is devoted to reviewing operations that may be relatively efficient and effective. As a result, our audit reports are prepared on an "exception basis." This report, therefore, highlights those areas needing improvement and does not address activities that may be functioning properly.

Response of SUNY Officials to Audit

A draft copy of this report was provided to SUNY officials for their review and comment. Their comments have been considered in preparing this report and are included as Appendix B.

Within 90 days after final release of this report, as required by Section 170 of the Executive Law, the Chancellor of the State University of New York shall report to the Governor, the State Comptroller, and the leaders of the Legislature and fiscal committees, advising what steps were taken to implement the recommendations contained herein, and where recommendations were not implemented, the reasons therefor.

Lease Practices

The Center, which includes the University Hospital, is located in what is known as the University Hill (Hill) area of Syracuse. Center officials indicate that it is generally necessary to locate Center and Plan space close to the Hospital in the Hill area to provide effective and convenient patient services and to minimize travel time for students, instructors and clinical practitioners. Center officials stated that, by meeting these objectives, the Center is competitive and capable of generating the revenues needed to support its mission and financial viability. However, the need for proximity may also create a real estate market demand which could put the cost for leased space in the Hill area at a premium. Therefore, in making leasing decisions, Center and Plan officials must maintain a proper balance between the benefits of locating in the Hill area and the cost of doing so. Adequate controls over leasing practices are essential to guide officials in making such lease decisions, and to provide assurance that leases obtained are both appropriate and reasonably priced.

As a result of our audit of Center and Plan leasing practices for the period April 1, 1993 through June 30, 1995, we concluded that documentation is not adequate to definitively determine whether or not the Center and the Plan paid reasonable lease costs. However, our audit did find a number of control weaknesses in Center and Plan leasing practices. For example, the Center:

- did not use competitive bidding to secure leases until 1995;
- has inadequate documentation to support its lease decisions;
- does not use available State or third-party experts in making lease decisions; and
- has no conflict of interest policy to ensure the propriety of lease decisions.

Our audit also shows that, for 13 of the 32 existing Plan and Center leases, the landlord is also a State employee who works for the Center or is an employee of the Plan which is affiliated with the Center. The amount of lease payments incurred in these instances totaled $1.8 million in 1994. We believe that these circumstances coupled with the control weaknesses increase the risk that the State and the Plan may be paying more than they should for leased space.

Center officials maintained that all lease rates were reasonable as supported by an independent appraisal for one location. However, we do not believe that an appraisal can establish the reasonableness of Center and Plan leases given the potential conflict of interest and leasing control weaknesses which existed.

Lease Costs

The use of competitive bidding for leases helps to ensure that rates paid are reasonable and that the lease award is fair. Moreover, the State Public Officers Law requires competitive bidding in those instances involving a conflict of interest, such as when a State employee is the landlord for space sought by the State. However, Center officials state that, historically, neither the Center nor Plan leases were obtained through competitive bidding. Essentially, whenever the Plan medical groups determine that they need more space to treat patients, the associated medical group determines the space requirements, suitable location and acceptable lease terms. Center management participates in the approval of these leases, but provides no official authorization since these leases are under the auspices of the Plan and are not "State" leases. Whenever Center funds are used to acquire space, the medical group involved finds suitable property and negotiates a lease with the formal involvement and approval of Center management, as is required for these State leases.

The need for competition for State leases arises from the direct concern that taxpayer dollars be utilized in an economical manner. In the case of Plan leases, taxpayers have an indirect interest in lease costs because, according to SUNY Policy, any Plan monies not required for Plan operations are to be used to benefit the State-funded School of Medicine. Therefore, to the extent that Plan lease costs are minimized, there is a potential for increased funding to meet State needs.

The following chart lists the average annualized costs for space at six properties leased by the Center and the Plan in the Hill area in 1994. The list accounts for 7 of the 17 Center leases and 15 Plan leases.

Property	State Costs	Plan Costs
Crouse-Irving Physicians Building	$25.36	$27.36
Harrison Center	$23.73	$24.88
Madison-Irving Building	*N/A*	$25.51
Hill Medical Building	*N/A*	$19.50
936 East Genesee Street	$22.33	*N/A*
Corporate Center	$18.02	*N/A*
N/A - No leases during 1994.		
(Note: The lease costs shown do not include costs for parking which is about $1.75 per square foot at many of the locations.)		

OGS and the Syracuse Chamber of Commerce report that the average cost of leased commercial property in downtown Syracuse (about one-half mile from the Hill area) is about $15 per square foot. Center officials state that our cost comparisons are not adequate because of the unique nature of medical space and the need for space which is proximate to the Center. We understand that the cost of medical space in the Hill area may exceed the $15 commercial rate; however, the absence of competitive bidding diminishes assurance that the lease costs are justifiably above the commercial rate. Moreover, the lack of competitive bidding may violate the Public Officers Law with respect to the leases in which the landlord is also an employee of the State.

In 1995, the Center did seek competitive bids in the negotiation of a space lease. As a result of this competition, the Center accepted a bid for 40,000 square feet of space for a base cost of $17 per square foot at the Corporate Center which is located near the Center. The cost to renovate this space will add another $8 to $9 per square foot to the total cost. However, at the end of five years, the rates will be reduced to the $17 base cost per square foot plus any increase in operating costs over the base year. This competitively bid lease compares favorably with non-competitively bid leases at other locations where lease costs have continued to be well in excess of $20 per square foot for a number of years.

Center officials indicate that this lease is unique because a significant volume of space was obtained.

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Documentation

The lease decision-making process must be fully documented, given the environment at the Center. If locating medical space in particular areas is determined to have a revenue impact, that impact should be quantified and included in documentation surrounding lease decisions. However, we found no revenue projection documentation or market studies to support either the need to locate in particular buildings or the need to be in the Hill area. The need for such documentation became more apparent when we examined particular leases in more detail.

For example, we noted that the Department of Preventative Medicine had paid about $22.50 per square foot for leased space in the Harrison Center, a Hill area building in which two State employees have an ownership interest. Subsequently, the Department moved to another location where the base lease rate was only $14 per square foot. In addition, we observed that some Center departments have secured leases at the average or less than the average rate for commercial space in Syracuse. The Family Medicine group leases medical space in DeWitt which costs the Plan $17 per square foot. Also, we noted that a realtor offered the Center space at $12 per square foot in a building which houses some medical facilities. While these sites are not close to the Hospital, the sites do accommodate medical space. Center officials stated that less costly suburban leases are obtained whenever it is appropriate to do so for the medical service being provided. Documentation, including revenue impacts, should fully justify why such less expensive space can not be obtained in lieu of more expensive space in the Hill area. This will ensure the careful analyses of all options and the most informed decision making.

Conflict of Interest

A conflict of interest policy helps to identify and control situations which could lead to actual or perceived ethical misconduct. We found that Center leases have evolved without the benefit of a conflict of interest policy or related procedures to govern the execution of leases with parties who are State employees or who may otherwise be in a position to influence leasing decisions in which the State has a financial interest. SUNY officials point out that on July 27, 1995, the SUNY Board of Trustees adopted a University wide conflict of interest policy. They add that conflict of interest provisions of the New York State Public Officers Law pertain to SUNY.

As is mentioned in the next section of this report, we found that the Center is leasing space that is owned in part by individuals with close ties to the Center. These relationships could have an adverse effect on the State by increasing rates the Center is paying. The absence of a

clearly articulated and consistently followed conflict of interest policy increases this risk.

Leasing Experts

Both Plan and State space leases at the Center are negotiated and finalized without assistance from independent experts such as the staff available at OGS or another third party. Given the previously mentioned weaknesses in the leasing control environment, such assistance would be useful to ensure necessary, independent expertise for assuring only reasonable prices are paid for space.

Appearance of Impropriety

The State Ethics Commission (Commission) was created as a result of the Ethics in Government Act (Act). The stated purpose of the Act is to restore the public's confidence in government and in government employees. The overall goal in passing the ethics law was ***to avoid the appearance of impropriety*** when conducting State business.

Pursuant to the Act, the Commission published a Code of Ethics covering ethical behavior for State employees. The Code of Ethics, which is issued to all employees, instructs employees to refrain from using their official positions to secure unwarranted privileges. The Code of Ethics also states that an employee not act as an agent for the State with any firm in which he or she has a financial interest which might tend to conflict with official duties. Further, an employee must avoid making personal investments in enterprises that might create a conflict of interest.

We found that some of the owners or managers of all of the buildings mentioned in the preceding chart have some relationship to the Center in addition to a landlord-tenant relationship. These individuals are State employees, Plan employees, former State or Plan employees, or members of the Board of Trustees for the Center's Foundation. We identified 32 such owner/managers, most of whom are listed as regular faculty or clinical faculty in the Center's current catalog.

We found that five of the owner/managers were State employees, one is the chairperson of a medical service group and three were employed by the Plan. The degree to which these individuals may influence decisions made by Center management cannot be determined. For example, the Harrison Center is currently owned by two members (including the chairman) of a medical service group. In 1994, the Plan and the Center paid $1.4 million ($24.66 per square foot) to rent space in the Harrison Center. This cost is significantly higher than the $17 per square foot rate which the Center recently obtained for property across the street

from the Harrison Center. The Center secured the lower rate as a result of the competitive bidding process.

Center officials told us that the building's ownership was not a factor in the decision. They stated that the Harrison Center space was needed to alleviate overcrowding in the Hospital, and that the decision to lease this space was based solely on need.

Compliance Issues

The Public Officers Law (Section 73) prohibits State employees who own a business from doing business with the State when the value of the service is over $25, unless the service is provided after public notice and competitive bidding. We found that none of the leases in effect during 1994 were competitively bid. However, as previously discussed, the Center did solicit bids on a new lease at the Corporate Center and accepted a bid to lease space for $17 per square foot.

The Public Officers Law also prohibits employees from appearing before a State agency for compensation in connection with the lease of real property. We found that the chairman of one of the departments signed several State and Plan leases as an owner of the building. It appears that this person also represented the owners in the negotiations for the lease. This situation suggests that the individual could use his involvement to influence the terms of the agreement. We are referring this situation to the Ethics Commission for an official ruling.

The SUNY Policy that governs the operation of the Plans at SUNY-operated hospitals limits the salary a physician employee may earn. The Policy caps physician salaries at 250 percent of their State salary. Physicians who own buildings may be circumventing the Policy by generating rental income. This is especially true when the owners lease space to the medical service group to which they belong.

Center management has been aware of the fact that persons with affiliations to the Center own or operate some of the buildings that lease space to the Center. These managers are also aware of the Act, the Code of Ethics and SUNY Policy. However, until recently when Center officials competitively bid space for the first time at the Corporate Center, they had not taken steps to ensure that lease transactions were free from the appearance of impropriety and the potential for violating State law.

Recommendations

1. Strengthen space leasing practices by adopting the control procedures identified in this report. Reevaluate existing lease arrangements to ensure that terms and conditions are reasonable.

2. Determine if the State Ethics Law and/or SUNY Policy has been violated in any Center or Plan lease arrangements and take steps to correct any such violations.

3. Consider alternative procedures for identifying and contracting for rental space, such as competitive bidding or the use of a third party in negotiating leases.

Renovation Cost Controls

Since 1990, the Center has spent nearly $1.8 million to renovate leased space. Some of these costs were paid by the Center (using State-appropriated funds) and some were paid by the Plan. We found that Center controls over the State leasing process are not adequate to prevent the State from being at an economic disadvantage when renovating leased space. Our review showed that the Center's procedures do not provide adequate information upon which to determine the value of proposed renovations, and that the lease terms may not protect the State's investment. In addition, both the State and some groups in the Plan rely heavily on the landlords to determine the cost of renovation projects. As noted earlier, some of these landlords work for the Center or the Plan, or have other affiliations with the Center.

Lease Negotiation Procedures

When the Center leases space, it is reasonable to expect that some renovations will be needed to accommodate the intended tenant. In the case of medical clinic space, the renovations may be extensive and costly. However, according to OGS, which is responsible for negotiating leases for space for State agencies throughout New York State, it is also reasonable to expect the landlord to pay for some renovation costs. It is also normal to expect that if the landlord incurs the cost of the medical upgrade, he will pass the costs incurred on to renters such as the Center. However, when we looked at the costs incurred to renovate some of the leased space, we found that the Center and the Plan were paying for nearly all of the upgrades. For example, a current Center lease at the Hill Medical Building requires renovations costing $150,000, all of which will be paid for by the Center at the beginning of the lease.

A description of the scope of renovation work should be incorporated in the lease along with the associated cost to the tenant to ensure a clear understanding of the work to be performed. We submitted descriptions of some Center renovation projects to OGS officials to obtain their appraisal of the value of the work performed. OGS told us that, in each case, the level of detail was insufficient to make a judgment about the worth of the project. However, we found that in most State leases this description is the only information available in Center records. According to the terms of many of these leases, the landlord decides on an architect and a contractor, and maintains relevant information (such as architect drawings and detailed specifications). Therefore, even though the State is paying for the project, Center documentation does not include the data needed to support decisions about how the money is spent.

Further, Center officials said that the Center usually does not require the landlord to obtain bids on the renovation projects. This practice may result in the Center paying more than necessary for renovations. We found that on one project where the landlord did obtain three bids, one of the three bidders complained that he was asked to bid based on a scope of work that was not sufficiently detailed to allow him to make an accurate bid. His bid was 32 percent above the low bidder; the other unsuccessful bidder bid 26 percent above the low bidder. The low bidder on this project was the landlord's usual contractor. This situation raises questions as to the propriety of how landlords award contracts for renovation projects.

We also found that the Center's procedures for negotiating renovation projects risk additional and possibly unnecessary costs. For example, we reviewed lease negotiations related to the Center's lease of space in the Hill Medical Building, including the agreement to pay $150,000 for renovations to convert space to a perinatal clinic. Center officials told us that the person responsible for negotiating the lease terms was the doctor who will head the clinic. To reduce the risk of additional and/or unnecessary costs, Center management should have monitored the progress of negotiations to ensure that renovations would result in an economic use of State funds. Center officials became involved only after agreements were substantially complete.

We also found that the certified architect on the Center staff is not always consulted about design and cost issues until after project agreements have already been reached between the Center and the landlord. For the above clinic project, the Center's architect was sent a summary of the project costs and asked to evaluate the scope of the proposed work after agreements about the renovations had already been reached. After reviewing the summary, the architect responded that some aspects of the project were not worth the price being charged and the description of other costs was too vague to make an accurate evaluation. Despite the architect's comments, the Center finalized the lease at the $150,000 price and began the renovation work. After the work was completed according to the plans, the Center found it could not open the clinic until additional renovation work was done. The Center estimates that the additional work will cost $10,700.

On another renovation project, the State had to pay $22,390 to rework some of the plumbing. The original work did not meet Department of Health codes. OGS told us that this rework would have been the responsibility of the architectural firm if the Center had a certified architectural drawing of the project. However, the Center did not obtain

such drawings. As a result, the Center (i.e., the State taxpayers) had to pay for the rework.

We also found that some of the Center's renovation projects include work that OGS officials indicated should be the landlord's responsibility. Examples of this type of work would include lighting, floor covering, painting and some wall finishing. During the course of our review, we did find that on some projects the landlord paid for some of these renovation costs. However, because the Center's documents do not include adequate detail, we cannot be sure which areas of the renovations are covered in the Center's lease payments and which are paid by the landlord.

Lease Terms

OGS also stated that leases should be of sufficient duration to protect the State's investment in renovation costs. For example, the leases should either have a long duration or include provisions to renew at specified rates. A longer lease lowers the average yearly cost of renovation and helps the tenant avoid the costs of renovating new space after a short-term lease expires.

We found three examples in which the Center or the Plan spent substantial amounts to renovate space without negotiating adequate renewal terms. For example, the renovation project for the perinatal clinic is part of a three-year lease. The lease includes a renewal provision, but the provision does not specify any renewal rate. Therefore, the landlord is not obligated to renew at terms agreeable to the Center. Should another tenant be willing to pay more for the newly renovated space, the State would be forced to either compete for the space it had already paid to renovate, or pay to renovate another site. We also found that the Center paid $139,649 for renovations at a site on East Genesee Street, and that a Plan group paid $78,621 for renovations at a site in the Harrison Center. Both of these leases are for five years and there are no renewal terms in either lease.

OGS officials also told us that landlords should derive their income from renting space and not from charging tenants high rates for money borrowed to fund renovation projects. When OGS officials negotiate State leases, they try to obtain interest rates for renovation work at or near the prime lending rate. We found two State leases in which the Center agreed to pay the landlord interest rates that were above the prime rate at the time the leases were signed.

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On a lease dated August 1990, the Center agreed to pay the landlord 12 percent interest to finance a $156,750 renovation project. The prime lending rate at the time was 10 percent. We calculated that if Center officials had agreed to pay interest at 10 percent, they would have saved $9,378 on this lease. On the second lease the Center agreed to pay interest at 11 percent when the prime rate was 8.5 percent. We calculated that on this $139,649 project the Center would have saved $10,271 if they negotiated at the prime rate.

We also found that two of the medical service groups in the Plan that lease space in the Harrison Center, agreed to pay interest at 14 percent for renovation work. The leases specify that if the landlord borrows money for general renovation work to the building, tenants will be billed for interest costs at 14 percent as part of operating cost escalations. We could not calculate how much interest the two groups paid to the landlord because the landlord does not itemize operating cost billings.

Recommendations

4. Establish renovation negotiation procedures that protect the State's interests, and use the services of professional personnel or third parties where practicable.

5. Obtain detailed documents to support planned renovation work.

6. Ensure that the duration of leases and/or renewal rates are adequate to protect the State's investment in renovation work.

7. Agree to pay finance charges at reasonable interest rates, at or near prime.

Major Contributors to This Report

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MAR 7 1996

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March 5, 1996

Mr. Robert H. Attmore
Deputy Comptroller
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The State Office Building
Albany, New York 12236

Dear Bob:

In accordance with Section 170 of the Executive Law, we are enclosing the comments of the State University of New York Health Science Center at Syracuse and SUNY System Administration regarding the draft audit report on Leasing Practices, State University of New York Health Science Center at Syracuse (95-S-80).

Sincerely,

William H. Anslow
Senior Vice Chancellor
for Finance and Management

Enc.

STATE UNIVERSITY OF NEW YORK
HEALTH SCIENCE CENTER AT SYRACUSE
LEASING PRACTICES
95-2-80

SUNY Health Science Center at Syracuse Comments

The audit states that "Although we could not definitively determine whether or not the lease rates paid were reasonable, we believe the Center's inadequate controls over leases may result in the State and Plan paying more than they should for leased space."

The Center contends that lease rates paid are clearly reasonable, and that the comparisons utilized by the auditors are not adequate.

The space noted on Page 4 of the draft is medical space proximate to the Hospital. The medical activities practiced in these areas are such that they must necessarily be near the Hospital. Proximity also serves as a convenience to the patients, thereby making the medical practice more marketable and allowing for the greater generation of revenues.

Unlike buildings in other city and county locations, those in the University Hill area are in high demand and are largely occupied. This results in higher rental rates than, for example, downtown properties. Also, the expenditures necessary to modify office space to medical space justify a higher rental rate.

The Comptroller's Office was provided with an expert independent appraisal of the rent at Harrison Center, which is comparable to the other rents noted on Page 4 of the report. The report, echoing the comments from the paragraph above, concluded that the rates paid at Harrison Center constitute economic rent for medical office space and is below the average cost of medical space in and around Syracuse.

If the Comptroller's Office took issue with the independent appraisal, it could have commissioned its own independent study, or performed a survey of real estate agents in the area. Instead they chose to include only those samples noted in the report.

The example of the Preventive Medicine Department is not relevant to the leasing of space in the Hill area. Due to the nature of its practice, Preventive Medicine found it could effectively operate in a suburban location. This allowed for a lower cost. In a like manner, the Health Science Center and the Plans have, when appropriate, rented space in less expensive suburban locations. The cost of these locations, which were not included in the report, was less than $15 per square foot.

The example of a realtor offering space to the Center at $12 per square foot is not sufficiently complete to constitute a valid comparable figure. While the building where the space was housed includes medical space, there is no indication that the space offered at $12 is medical space. Also, as noted in the report, the space is not proximate to the Center.

While the Center does acknowledge that it received a favorable rate of $17 through the bidding process, it also notes that the first five years of the lease will cost more nearly $26 to $27. Also the lease of this space was a unique opportunity for the Center, because of the significant volume of space which was rented at one time. This situation was not typical of the other rentals.

To reiterate, the Center believes that the space noted in the report was rented at a fair rate. The Center will, however, adopt written leasing policies to reinforce its leasing procedures. The Center will also competitively bid leases, where practical, and seek the assistance of outside parties in negotiating leases where appropriate. The Center will also encourage the Plans to follow like policies.

As regards the controls over renovation costs, the Center will continue its efforts to control costs. The two most recent lease contracts are both ten years in duration. Also, the Center requires drawings of all original construction, as well as documentation for any changes to the work. Architects on staff review both the drawings and the changes before work begins. Finally, the Center has recently employed extensive efforts to obtain low interest rates for construction projects.

In sum, the Center will employ its best efforts to follow the Comptroller's Office recommendations, where possible.

State University of New York Comments

Regarding the audit comments on:

- Page 2 of the Executive Summary, "we found that the Center has no conflict of interest policy to guide lease decision making".

- Page 3, Lease Practices, "the Center has no conflict of interest policy to ensure the propriety of lease decisions".

- Page 6, Conflict of Interest, "We found that Center leases have evolved without the benefit of a conflict of interest policy or related procedures to govern the execution of leases with parties who are State employees or who may otherwise be in a position to influence leasing decisions in which the State has a financial interest."

We offer the following comments:

The draft audit does not give sufficient recognition to the fact that the faculty and staff of the State University of New York are subject to the conflict of interest provisions of the New York State Public Officers Law. Also, on June 27, 1995, the Board of Trustees adopted a State University of New York Policy on Conflict of Interest (previously provided). Finally, the Procedure Manual items dealing with SUNY Purchasing and Contracting Procedures (APM Items 300 and 310) specifically state: "The Conflict of Interest and Code of Ethics provisions of Sections 73 and 74 of the Public Officers Law shall apply to all purchasing and contracting activities under these rules and regulations".

In the course of the State Comptroller's audit of the HSC Syracuse leases, it was discovered that in some instances the parties with whom the University was contracting were also employees of the State University. On its face, such relationship, if entered into without competitive bidding, could conflict with the provisions of §73 of the New York State Public Officers Law (POL).

POL §73(4)(a) states, in applicable part:

"(a). No statewide elected official, *state officer or employee*, member of the legislature, legislative employee or political party chairman or firm or association of which such person is a member, *or corporation, ten percentum or more of the stock of which is owned or controlled directly or indirectly by such person, shall (I) sell any goods or services having a value in excess of twenty-five dollars to any state agency,* or (ii) contract for or provide such goods or services with or to any private entity where the power to contract, appoint or retain on behalf of such private entity is exercised, directly or indirectly by a state agency or officer thereof, *unless such goods or services are provided pursuant to an award or contract let after public notice and competitive bidding....*" (emphasis added).

Section 73(1)(I) defines "state officer or employee" in part as follows:

"(I) heads of state departments and their deputies and assistants....";

... (iii) officers and employees of state departments, boards, bureaus, divisions, commissions, councils or other state agencies...."; and

(iv) members or directors of public authorities, other than multi-state authorities, public benefit corporations and commissions at least one of whose members is appointed by the governor, who receive compensation other than on a per diem basis, and employees of such authorities, corporations and commissions."

Finally, POL §73(1) defines "state agency" in applicable part as:

"... any state department, or division, board, commission, or bureau of any state department...."

Under the definition above, and by judicial decision, the State University is a "state agency"; therefore the above provisions of the POL would apply to its contracts and leases.

In the lease review described above, it became clear that the HSC at Syracuse was unaware that some of those with which it was entering into leases were employees of the University as well. As leases are often not subject to formal competitive bidding in the same manner as other contracts, possible violations of POL §73 could have occurred. In order to reduce the likelihood of this in the future, we will modify the contracting procedures appearing as Item 300 of the University Procedures Manual.

Item 300, Part II(B) currently refers to POL §73, and a copy of POL §73 is attached to Item 300. However, a specific inquiry as to the status of those with whom the University contracts will now

also be made an initial part of the process of contracting and leasing. To such end, the following will be added as an Attachment to this Item:

> Please indicate if any officer of your organization, or any party owning or controlling more than 10 per cent of your stock if you are a corporation, or any member if you are a firm or association, is an officer or employee of the State of New York or of a public benefit corporation of the State of New York [ ] Yes [ ] No.

If the answer to such inquiry is in the affirmative, it will be necessary to use the formal competitive bidding processes generally applicable to University procurement, as described in Procedures Manual Items 300 and 310, before a valid agreement may be entered into with such individual or organization, in order to comply with the provisions of POL §73.

We expect to add the above to the Procedures Manual in a revision to be completed within the next few months.

We agree with the audit recommendations and the Health Science Center's response.